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BEFORE THE ARIZONA CORPORATION COMMISSION

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KRISTIN K. MAYES, Chairman
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ARIZONA CORPORATION COMMISSION
TICKET CONTROL

IN THE MATTER OF THE APPLICATION
OF LITCHFIELD PARK SERVICE
COMPANY, AN ARIZONA CORPORATION,
FOR A DETERMINATION OF THE FAIR
VALUE OF ITS UTILITY PLANTS AND
PROPERTY AND FOR INCREASES IN ITS
WASTEWATER RATES AND CHARGES
FOR UTILITY SERVICE BASED THEREON.

DOCKET NO. SW-01428A-09-0103

IN THE MATTER OF THE APPLICATION
OF LITCHFIELD PARK SERVICE
COMPANY, AN ARIZONA CORPORATION,
FOR A DETERMINATION OF THE FAIR
VALUE OF ITS UTILITY PLANTS AND
PROPERTY AND FOR INCREASES IN ITS
WATER RATES AND CHARGES FOR
UTILITY SERVICE BASED THEREON.

DOCKET NO. W-01427A-09-0104

IN THE MATTER OF THE APPLICATION
OF LITCHFIELD PARK SERVICE
COMPANY, AN ARIZONA CORPORATION,
FOR AUTHORITY (1) TO ISSUE EVIDENCE
OF INDEBTEDNESS IN AN AMOUNT NOT
TO EXCEED \$1,755,000 IN CONNECTION
WITH (A) THE CONSTRUCTION OF TWO
RECHARGE WELL INFRASTRUCTURE
IMPROVEMENTS AND (2) TO ENCUMBER
ITS REAL PROPERTY AND PLANT AS
SECURITY FOR SUCH INDEBTEDNESS.

DOCKET NO. W-01427A-09-0116

Arizona Corporation Commission

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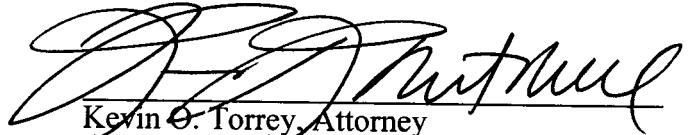
IN THE MATTER OF THE APPLICATION
OF LITCHFIELD PARK SERVICE
COMPANY, AN ARIZONA CORPORATION,
FOR AUTHORITY (1) TO ISSUE EVIDENCE
OF INDEBTEDNESS IN AN AMOUNT NOT
TO EXCEED \$1,170,000 IN CONNECTION
WITH (A) THE CONSTRUCTION OF ONE
200 KW ROOF MOUNTED SOLAR
GENERATOR INFRASTRUCTURE
IMPROVEMENTS AND (2) TO ENCUMBER
ITS REAL PROPERTY AND PLANT AS
SECURITY FOR SUCH INDEBTEDNESS.

DOCKET NO. W-01427A-09-0120

**NOTICE OF FILING
STAFF'S REPLY BRIEF**

1 The Arizona Corporation Commission ("Commission") Utilities Division Staff ("Staff")
2 hereby provides its reply brief in the above-referenced matters.

3 RESPECTFULLY SUBMITTED this 25th day of February, 2010.
4

5 
6

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13 25th day of February, 2010, with:

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1 The Utilities Division ("Staff") of the Arizona Corporation Commission ("Commission")
2 responds as follows to the closing briefs filed by Litchfield Park Service Company ("LPSCO" or the
3 "Company"), the Residential Utility Consumer Office ("RUCO") and the City of Litchfield Park
4 ("City"). The purpose of this Reply Brief is not to repeat every point made in Staff's Initial Closing
5 Brief, nor will it attempt to refute every single issue raised by LPSCO, RUCO or the City; instead
6 Staff relies upon its testimony on those issues not specifically addressed in this Reply Brief. The
7 recommendations of Staff and its positions have been outlined in its Closing Brief as well as its
8 testimony. Staff will highlight some of the major points of disagreement with the Company in this
9 brief.

10 **I. RATE BASE ISSUES.**

11 **A. Staff's ADIT calculation is reasonable and should be adopted.**

12 Accumulated deferred income taxes ("ADIT") reflect the timing difference between when
13 income taxes are calculated for ratemaking purposes and the actual federal and state income taxes
14 paid by the Company.¹ The timing difference is primarily due to the fact that straight line
15 depreciation is used for ratemaking purposes, whereas accelerated depreciation is used for income
16 tax reporting purposes. The Statement of Financial Accounting Standards ("SFAS") No. 109,
17 Accounting for Income Taxes, requires companies to use deferred tax accounting to recognize
18 income tax timing differences.²

19 The Company complains that Staff's ADIT calculation is unsupported by substantial
20 evidence and should be disregarded.³ Staff adopted the Company's deferred income tax numbers
21 found in its 2008 Annual Report.⁴ Staff attempted to work with the Company to determine the
22 methodology it used to calculate its ADIT but the Company's number was a moving target.

23 At the time of filing of its Rejoinder testimony on December 29, 2009, the Company was still
24 updating its number, with the hearing just days away. According to Staff witness Jeff Michlik, the
25 Company changed its ADIT numbers three times.⁵

26
27 ¹ Decision No. 69164 at 5.

28 ² *Id.*

³ LPSCO Reply Brief at 41.

⁴ Ex. S-20; Ex R-7; Tr. 1159-1160.

⁵ Tr. at 1159:6-9.

1 The Company was unable to provide an adequate reconciliation of any of the proposed
2 calculations. Furthermore, Mr. Michlik testified that even the Company's external auditors, KMPG,
3 derived a different number than that of the Company's witness, Mr. Bourassa.⁶ LPSCO complains
4 that the annual report number should be disregarded because the annual report date does not match
5 the test year. However, the Company's test year amount was identical to the amount the Company
6 submitted in its 2008 annual report, despite being three months beyond the test year.⁷ Therefore,
7 Staff believes the Company's test year ADIT number to be the more reliable.

8 **B. Security Deposits.**

9 The Company asserts that Staff did not follow the prescribed accounting treatment for
10 customer deposits.⁸ This assertion is incorrect.

11 Staff witness Michlik states that Staff's treatment was in accordance with the prescribed
12 accounting treatment as expressed in the following section of Matthew Bender & Company's
13 publication, *Accounting for Public Utilities*::

14 **Customer deposits generally represent funds received from ratepayers as**
15 **security against potential losses arising from failure to pay for service. These**
16 **funds are similar in nature to customer advances for construction. Both**
17 **represent a liability to repay the funds received either after a specified period or**
upon satisfaction of certain requirements. Like customer advances, the deposits
are available to the utility for use in support of its rate base investment.

18 The alternative methods of treating customer deposits for ratemaking purposes also
19 parallel the treatment of customer advances. If no interest accrual is required on the
20 funds, the deposits represent a cost-free source of capital commonly deducted from
21 the rate base. If customer deposits are interest bearing, two options are available.
22 The liability may be deducted from the rate base with the associated interest included
as a component of cost of service, or the liability may be included in the capital
structure for purposes of calculating the allowed rate of return (in which case there is
no rate base reduction).⁹ (emphasis added).

23 Staff's position is also supported by the *Rate Case and Audit Manual*, prepared by NARUC Staff
24 Subcommittee on Accounting and Finance (2003):

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28 ⁶ Tr. at 1225:1-9.

⁷ Tr. at 1223:19-25; 1224:1-12.

⁸ Company Brief at 43.

⁹ Ex. S-18.

1 Customer deposits are shown as a liability on the utility's balance sheet and represent
2 a source of non-investor supplied capital. Customer deposits are generally treated one
3 of three ways.

4 The first method does not reduce rate base by the customer deposits balance and
5 classifies any interest accrued or paid on those deposits as a below-the-line (or non-
6 operating) expense. This method allows the utility to earn a return on a rate base that
7 has not been reduced by the amount of customer deposits, and then allows it to use
8 that return to pay the interest that is required to be returned to customers with the
9 return of that deposit. One consideration in using this method is whether the return
10 allowed on rate base is higher than the return that the utility is required to pay on its
11 customer deposits. If so, the utility may be allowed to earn more than is necessary,
12 and return that difference to shareholders.

13 The second method reduces rate base by the customer deposits balance, and classifies
14 any interest accrued or paid on those deposits as an above-the-line (or operating)
15 expense that is included in the revenue requirement computation. The interest that the
16 utility must pay is generally deemed to be a legitimate expense that must be recovered
17 in one form or another.

18 The third method includes the liability for customer deposits in the utility's capital
19 structure at a zero cost, reducing the overall rate of return. If interest is paid on the
20 customers' deposits, the utility can recover that interest expenses as an above-the line
21 (or operating) expense.¹⁰

22 Staff followed the approved methodology as recommended by the utility regulatory
23 profession, by reducing the rate base by the amount of customer deposits and making a
24 corresponding adjustment to operating expense. Staff relied on the dollar amounts provided by the
25 Company to make these entries in its final schedules.¹¹

26 As was noted by Mr. Michlik's testimony, there is no differentiation between meter deposits
27 and security deposits as the Company claims,¹² and the Company has not produced any authoritative
28 source such as NARUC or a Utility Ratemaking reference or manual to support its claim.

29 The Company further criticizes Staff's methodology for "fail[ure] to offset the Accounts
30 Receivable balances associated with the security deposits included in rate base."¹³ The Company
31 suggests that the customer deposits should be netted against the accounts receivable for those
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¹⁰ Available at http://www.naruc.org/Publications/ratecase_manual.pdf.

¹¹ Staff's final schedules.

¹² Tr. at 1154-1155; Exs. S-18 and S-19.

¹³ Company Brief at 43:5-7.

1 customers. Staff disagrees with this position for two reasons: 1) There is no rate-making literature
2 to support this position, and 2) the Company did not perform a lead-lag study to support the
3 recognition of accounts receivable in rate base.

4 In line with generally-accepted ratemaking principles, Staff has consistently treated customer
5 deposits as a reduction from rate base.¹⁴ To do otherwise would unfairly allow the Company to earn
6 a return on money that is not its own.

7 **C. Deferred Regulatory Asset.**

8 Staff believes the deferred costs related to the Trichloroethylene ("TCE") plume are not ripe
9 for adjudication and should continue to be deferred until a future rate case, as there are still too many
10 unknowns at this time.¹⁵ The Company, on the other hand, suggests that ratepayers should assume
11 the burden of these costs. Staff believes the intent of Decision No. 69912 was to hold ratepayers
12 harmless and place the burden on the responsible third parties.¹⁶ If the costs were shifted now to the
13 ratepayers and if the Company were to receive some type of future recovery or settlement from a
14 third party, it is uncertain if the ratepayers would receive any of the benefit.

15 If the Commission decides that the recovery should be made now from ratepayers, Staff
16 would recommend that the costs be recovered on a forward basis through traditional expenses such
17 as water testing and legal expenses, and that the accumulation of these deferred costs be eliminated.

18 **II. INCOME STATEMENT.**

19 **A. Central Cost Allocation.**

20 Contrary to the assertions of the Company, Staff is not opposed to a shared services model.¹⁷
21 In recognition that there may be a benefit to the ratepayer, Staff allowed 10 percent of the cost
22 allocation.¹⁸ The model proffered by Liberty Water (formerly Algonquin Water Resources of
23 America) is unique to the regulatory scheme in Arizona¹⁹ and the Company should not feign shock
24 and surprise that such a model would come under scrutiny by Staff, RUCO and the Commission.

25 ¹⁴ *In the Matter of the Application of Arizona Water Company*, Docket No. W-01445A-08-0607.

26 ¹⁵ Tr. at 1162:11-19.

27 ¹⁶ The final ordering paragraph ordered LPSCO to "actively assert the legal remedies available to
28 them from the party or parties responsible for the potential contamination of their water supplies."

¹⁷ Tr. at 1163:1-12.

¹⁸ *Id.*

¹⁹ Decision No. 69664 at 12.

1 The Commission placed Liberty Water on notice that its model would be scrutinized in its future rate
2 cases.²⁰

3 State Commissions have subjected affiliate transaction to a greater scrutiny. For example, in
4 *U.S. West Communications v. Arizona Corporation Commission*, 185 Ariz. 277, 915 P.2d 1232
5 (App. 1996), the Arizona Court of Appeals held that the "Commission has broad powers to
6 scrutinize transactions between a regulated company and its unregulated affiliates" and disallow
7 excessive costs.²¹ Sifting through all the rhetoric in the Company's brief, Staff simply wants to
8 ensure that the costs that are allowed are necessary for providing service and are reasonable.

9 Although the Company argues that its shared services model is cost effective, there is still
10 doubt as to the reasonableness of the expenses where a company such as LPSCO, has no ability to
11 negotiate in an arms length negotiation. In an open, competitive market, it is reasonable to assume
12 that contract prices reflect market prices. The reasonableness of affiliate costs should not rely
13 primarily on company assertions. Yet, LPSCO insists that the Commission rely solely on its
14 assertions that its expenses are reasonable.

15 In its Closing Brief, the Company asserts that its operating costs are in line with other
16 Arizona water and wastewater utilities, but yet it did not present this evidence at the hearing. In fact,
17 the Company was critical of Staff's comparison of operating costs for stand alone utilities with those
18 costs of LPSCO.²² LPSCO, in support of its central office cost allocation and the benefits received
19 by LPSCO by this method, relies on a paper presented by Company witness, Gerald Tremblay
20 entitled "Liberty Water Affiliate Cost Allocation Methodology."²³

21 The Company, in an attempt to bolster its argument that its shared services model lowers
22 costs, estimates that if it were not for the services provided by Algonquin Power Trust ("APT"),
23 LPSCO would need to hire ten employees. According to Company witness Tremblay, LPSCO
24 would need a payroll of over \$800,000 to replicate the services provided under its cost model. In this
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26

27 ²⁰ *Id.* at 23-24.

28 ²¹ *US West*, 185 Ariz. at 282, 915 P.2d at 1237 (citations omitted).

²² *Tr.* at 1175-1179.

²³ *Ex. A-9.*

1 era of “doing more with less,” such a payroll number seems unrealistic and excessive, calculated by
2 the Company to make its model seem more reasonable.

3 The Company, in a twisted reading of the substantial evidence rule, chastises Staff and
4 RUCO for failing to provide “substantial evidence to refute Mr. Tremblay.”²⁴ As the Company so
5 aptly notes, it bears the burden of proof.²⁵ Despite the inflammatory rhetoric used by the Company,²⁶
6 it has not proven that it is entitled to entirety of the cost allocation numbers requested. Self serving
7 and conclusory statements made by the Company witness are unpersuasive.

8 The very decision cited by the Company in support of allocation supports the Staff’s position
9 that it is appropriate to compare expenses with those of other water utilities. In disallowing certain
10 O&M expenses requested by APS, the Commission said “[a]s a very general rule, we believe that
11 industry data, particularly data from comparable companies, can be used to gauge the reasonableness
12 of a utility's costs.”²⁷ Thus Staff’s comparison to stand alone utilities finds support in Commission
13 decisions.

14 The attempt by the Company to include Super Bowl tickets, charitable contributions, tax
15 penalties and private jet allocations into the cost to be allocated to LPSCO under its shared services
16 model leaves Staff feeling less than confident that all the costs attempted to be allocated are
17 reasonable and necessary for the provision of service.

18 Staff, in making its recommendations, is not attempting to dictate how Liberty Water
19 manages its business.²⁸ This is not a question of how a utility can operate, but one of what
20 reasonable costs and expenses a utility should be allowed to be passed on to its captive ratepayers.

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25 ²⁴ Company Brief at 56.

26 ²⁵ Tr. at 1095:20-21.

27 ²⁶ Company Brief at FN 302, (“Frankly, it’s hard to believe Staff or RUCO can make that argument
with a straight face...”).

28 ²⁷ Decision No. 55931, 91 P.U.R.4th 338, 348.

²⁸ The Company cites *Southern Pac. Co v. Ariz. Corp. Comm’n.*, 98 Ariz. 339, 343, 404 P.2d 692,
695 (1965). *Southern Pacific* also held that the Commission, in the exercise of its regulatory power,
may interfere with the management of public utilities whenever the public interest demands.

1 **III. COST OF CAPITAL.**

2 **A. Response to City's Proposal.**

3 The City proposes that the Commission disregard Staff's, RUCO's and the Company's
4 recommendations for a return on equity. The City recommends that the Commission cap the
5 increase for both systems at a return of no more than 7.5% on fair value rate base.²⁹ While the City
6 correctly noted the Commission's plenary rate making authority, Staff is concerned that a record was
7 not developed to support the City's recommendation.

8 **B. Staff's return on equity is reasonable and should be adopted.**

9 Staff's recommendation of a 9.2% return on equity is reasonable, given the Company's
10 recommendation of 12.14%. The Company seems to complain that because there is debt in its
11 capital structure, it is subject to more financial risk than its sister company Black Mountain; yet the
12 Staff's calculation using the Hamada equation, resulted in a ROE that is 20 basis points lower than
13 Staff's recommendation in Black Mountain, a company that has no debt in its capital structure. The
14 Staff results are not incongruous as suggested by the Company, but stem from recognition of a
15 number of factors that differentiate LPSCO from Black Mountain. As noted by Staff witness Juan
16 Manrique, there is no set formula used by the Commission.³⁰

17 The Company simply ignores the relationship between economic conditions and the cost of
18 capital. The court held in *Bluefield*:

19 What annual rate will constitute just compensation depends upon many
20 circumstances and must be determined by the exercise of fair and
21 enlightened judgment, having regard to all relevant facts...A rate of
22 return may be reasonable at one time and become too high or too low
by changes affecting opportunities for investment, the money market
and business conditions generally.³¹

23 Although the Company's cost of equity recommendation was lower, at 12%, in rebuttal than the
24 14% it was seeking in its Direct testimony,³² the Company seems to imply that as a regulated entity,
25 it should somehow be shielded from the negative impacts of today's economy that affect its
26

27 ²⁹ City's Brief at 2.

28 ³⁰ Tr. at 1138:14.

³¹ *Bluefield Water Works v. Public Service Commission of West Virginia*, 262 U.S. 679 (1923).

³² Ex. A-17 at 3-4.

1 ratepayers and virtually every other business. The Company even notes that while the recession may
2 be over, economists see a long, sluggish recovery.³³ The Company's recommended cost of equity
3 of 12% is beyond the range of returns ordered by the Commission in the most recent rate orders.³⁴
4 Staff's cost of equity recommendation of 9.2% is consistent with recent Commission decisions and
5 will result in the setting of just and reasonable rates.

6 IV. RATE DESIGN.

7 A. Phased-In Proposal.

8 At the commencement of the evidentiary hearing in this case, Chairman Mayes requested that
9 the parties address a proposal for phased-in rates, regardless of the individual parties' actual
10 proposed rate increase.³⁵ All of the parties discussed their views of phased-in rates during the
11 hearing, and ultimately some of the parties submitted phased-in rate design alternatives with their
12 final schedules.

13 Based on past experiences with phased-in rates, Staff is concerned that while ratepayers may
14 enjoy lower rates in the short term, in the long term they will inevitably pay more than they would if
15 there was no phase-in of rates.³⁶ Even though the Company has now proposed a rate design that
16 consists of a phase-in, the Company acknowledged throughout the hearing that in the end, "the
17 customers end up paying a lot more in their rates."³⁷ As Company witness Mr. Bourassa explains,
18 the reason back end costs are typically so high is due to the requirement of having to make up for
19 forgone revenue and carrying costs during the phase-in period, thereby raising the rates
20 tremendously in the back end.³⁸ In the end, the ratepayer not only has to pay for the forgone
21 revenue, but also the interest the Company would have earned on that revenue, had it been collected
22

23 ³³ *Id.* at 3.

24 ³⁴ See Docket No. G-01551A-07-0504, *In the Matter of the Application of Southwest Gas*, Decision
25 No. 70665 (10 percent cost of equity); Docket No. G-04204A-06-0463, *In the Matter of the*
26 *Application of UNS Gas, Inc.*, Decision No. 70011 (10 percent); Docket No. W-01303A-08-0227, *In*
27 *the Matter of the Application of Arizona-American Water Company*, Decision No. 71410, (9.9
percent cost of equity); Docket No. W-02113A-07-0551, *In the Matter of the Application of*
Chaparral City Water Company, Decision No. 71308 (9.9 percent cost of equity).

28 ³⁵ Tr. at 33-34:22-7.

³⁶ Tr. at 1035:4-12.

³⁷ Tr. at 532:9-10, 532:14-17, and 531-2:25-5.

³⁸ Tr. at 531-2:25-5.

1 sooner. These are costs ratepayers would typically never incur if a rate were just directly
2 implemented.

3 The Commission may adopt the proposed phased-in rates if it concludes it is in the public
4 interest. While phased-in rates may provide the ratepayer with immediate relief from potential "rate
5 shock" today, the ratepayer could end up paying 129 percent over the Company's authorized rate. It
6 is difficult to foresee if the nation will experience a substantial economic recovery over the life of
7 the proposed three year phase-in. Because of this unknown, an attempt to avert a presently
8 perceived financial hardship through phased-in rates could actually create an even more serious
9 financial hardship in the future.

10 Another concern with the Company's proposed phased-in rates³⁹ discussed during the
11 hearing and in the closing briefs is what happens during year four, after the phased-in period is
12 complete.⁴⁰ The Company's Closing Brief suggested that either the rates automatically revert to the
13 100 percent authorized rate or the Company should be required to file a rate application. Both
14 options have their own sets of concerns. If the rate is to automatically revert back, there are
15 monitoring and compliance issues. If a rate case is required, it raises the questions of what
16 constitutes an appropriate test year and what rates should be charged during the pendency of the rate
17 proceeding. The Company's proposal does not adequately address these concerns. Should the
18 Commission decide to adopt phased-in rates, it is important that any Commission decision address,
19 in detail, what will happen at the end of the phasing-in process.

20 The Company states that its acceptance and promotion of phased-in rates is not conditional
21 on its own proposed revenue requirement being adopted; the Company does not oppose applying
22 phased-in rates to whatever revenue requirement is ultimately adopted.⁴¹ However, Staff notes that
23 under Staff's recommended revenue requirement there would be less of a "rate shock," mitigating
24 any need for phased-in rates.

26
27 ³⁹ RUCO, in RUCO's Final Post Hearing Schedule at 87-8, provided a proposal for phased-in rates.
28 While the numbers and time frame are different than the Company's proposal, Staff's general
objections are still applicable.

⁴⁰ Tr. at 531-2:25-5.

⁴¹ Tr. at 1382-9:25-1.

1 Whether or not phased-in rates are appropriate in the instant case and should be adopted is a
2 policy decision for the Commission. Staff urges the Commission to consider not only the increased
3 costs incurred by ratepayers in the long run, but also the unknown economic conditions of the future.
4 In the instant case, Staff advises caution in the decision to adopt the Company's rate design proposal.

5 **B. Staff's rate design is reasonable, promotes the efficient use of water and should**
6 **be adopted.**

7 Staff disagrees with the Company's assertion that "water conservation is simply a smoke
8 screen to justify ignoring cost of services principles."⁴² There are rates that were previously approved
9 by the Commission that were not based strictly on the cost of service. The Commission, in Decision
10 No. 60172, notes that cost of service studies are simply "tools" for establishing revenue requirement
11 per customer class.⁴³ Staff agrees cost is a factor, but only one of various factors considered in the
12 development of a rate design.⁴⁴

13 Contrary to the Company's assertions, the rate design advanced by the City and the Company
14 does not promote conservation. The breakpoints for the ¾ inch meter are 15,000 gallons, the next
15 breakpoint is at 35,000 gallons and the third breakpoint is 50,000 and over.⁴⁵ For the 1 inch meter,
16 the breakpoints are even wider 15,000 gallons and the next breakpoint is at 85,000 gallons and the
17 third breakpoint is 100,000 gallons.⁴⁶ These proposed breakpoints are above the current usage
18 reported for these customers in the classes, thus providing no incentive to use less water. As the ALJ
19 noted, the Commission has not seen breakpoints such as these in all his years at the Commission.⁴⁷
20 Staff could not find any rate designs in recent Commission decisions which approved the types of
21 tiers being proposed by the City and the Company. Further, the Company's rate design is deficient
22 in that it has inequitable crossovers, i.e., usage levels at which the bill for a smaller meter is higher
23 than the bill for a larger meter.⁴⁸ The rate designed as proposed by the City and the Company should
24 be rejected.

25 _____
26 ⁴² Company's Brief at 82.

27 ⁴³ See Decision No. 60172 at 40, 43-44.

28 ⁴⁴ Ex. S-3 at 8-9.

⁴⁵ Ex. LP-4.

⁴⁶ *Id.*

⁴⁷ Tr. at 663-664.

⁴⁸ Tr. at 1036-38.

1 **C. City of Goodyear Public Comment.**

2 The City of Goodyear ("Goodyear") in a letter dated February 10, 2010, and docketed
3 February 19, 2010, requested, among other things, rates not be set in this case for bulk water but be
4 subject to negotiation between Goodyear and LPSCO. Goodyear asserts that, in an effort to assist in
5 the TCE plume clean-up and without any legal requirement to do so, it has donated its property,
6 easements and rights-of-way for the drilling of monitoring and extraction wells and construction of
7 main treatment systems. According to Goodyear, because these assets and services have not been
8 properly valued, Goodyear should be allowed to negotiate a bulk water rate with LPSCO. However,
9 Staff notes that the authority of setting of rates lies with the Commission. Further, Goodyear's
10 comments support Staff's position regarding the deferred costs related to the TCE plume.⁴⁹

11 **V. FINANCING APPLICATIONS.**

12 The Company has applied for authorizations to finance a solar energy project at its Palm
13 Valley Water Reclamation Facility and an effluent recharge facility.⁵⁰ During the hearing, the
14 Company indicated that it may change the recharge technology from what was contained in its
15 application. As Staff witness Marlin Scott testified, any such change would require Staff to review
16 both the costs and the recharge method.⁵¹ Mr. Michlik testified that an order that allowed the
17 Company some flexibility, along with Staff review of any modification, would be acceptable to
18 Staff.

19 A review of the Commission's order in Decision No. 69238 is instructive.⁵² The
20 Commission granted Arizona Electric Power Cooperative, Inc. ("AEPCO") financing authorization
21 in the amount of approximately \$29.2 million for the completion of its authorized construction work
22 plan. AEPCO sought the ability to make minor modifications to its work plan without filing an
23 amended application. The Commission granted AEPCO's request, limiting the amount of the
24 modifications to \$500,000 and requiring AEPCO to submit the modifications to the work plan for
25

26 ⁴⁹ See February 10, 2010 letter from City of Goodyear at p. 6 , docketed in this docket February 19,
27 2010.

28 ⁵⁰ Company Brief at 87.

⁵¹ Tr. at 1112:4-25.

⁵² Docket No. E-01773A-06-0084, In the Matter of the Application of Arizona Electric Power
Cooperative, Inc.

1 Staff review. As the Decision noted, “[t]he statutes that give the Commission authority to approve
2 finance requests require as a prerequisite to approval that the Commission find the financing request
3 to be reasonably necessary or appropriate for the purposes specified in the order. A.R.S. §40-302.
4 We cannot make a finding of reasonableness or appropriateness without knowing the purposes of the
5 financing request.” But the Commission went on to find that because AEPCO was willing to submit
6 its modifications to Staff prior to making them and because of the minor amount of modifications
7 allowed relative to the entire amount approved, AEPCO should be allowed some flexibility and
8 allowed AEPCO to make changes that conform to purposes of the approved work plan.

9 VI. ECONOMIC CONDITIONS.

10 The Company appears to argue that the Commission is limited in the factors it can consider
11 when setting just and reasonable rates. Staff would caution against such a narrow interpretation of
12 the Commission’s plenary rate making authority.

13 Article 15, section 3, of the Arizona Constitution provides, in relevant part, that the
14 Commission “shall have full power to, and shall, prescribe just and reasonable classifications to be
15 used and just and reasonable rates and charges to be made and collected by public service
16 corporations within the State for service rendered therein.” In determining just and reasonable rates,
17 the Commission has broad discretion, subject to the obligation to ascertain the fair value of the
18 utility’s property and to establish rates that “meet the overall operating costs of the utility and
19 produce a reasonable rate of return.”⁵³ Under the Arizona Constitution, a utility company is entitled
20 to a fair rate of return on the fair value of its properties, “no more and no less.”⁵⁴ Arizona law does
21 not mandate that the Commission (1) follow a particular method in its rate making determinations or
22 (2) exclude consideration of relevant factors.⁵⁵

23 The Company argues that it is impermissible for the Commission to consider the current state
24 of this nation’s economy in the setting of just and reasonable rates. Protecting ratepayers, however,
25 is part of the balancing in the public interest performed by the Commission. The Commission not
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27 ⁵³ *Scates, et al. v. Arizona Corp. Comm’n*, 118 Ariz. 531, 534, 578 P.2d 612 (App. 1978).

28 ⁵⁴ *Litchfield Park Service Co. v. Arizona Corp. Comm’n*, 178 Ariz.45 I, 434, 854 P.2d 988 (App. 1994) (citing *Arizona Corp. Comm’n v. Citizens Utilities Co.*, 120 Ark. 184 (App. 1978)).

⁵⁵ *Simms v. Round Valley Light & Power Company*, 80 Ariz. 145, 151, 294 P.2d 378, 382 (1956).

1 only sets just and reasonable rates for public service corporations, but also sets rates to protect
2 ratepayers from overreaching by those very corporations.⁵⁶ The Company's arguments are no more
3 than an attempt to undermine the Commission's balancing of customer and utility interests at the
4 expense of ratepayers. "The jurisprudence of our state made it plain long ago that the interests of the
5 public service corporation stockholders must not be permitted to overshadow those of the public
6 served."⁵⁷

7 **VII. CONCLUSION.**

8 Staff respectfully requests the Commission to adopt its recommendations in this proceeding.
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⁵⁶ *Scates v. Arizona Corporation Commission*, 188 Ariz. 531, 534, 578 P.2d 612 (App. 1978)

26 ⁵⁷ *Ariz. Community Action Ass'n v. Ariz. Corp. Comm'n*, 123 Ariz. 228, 231, 559 P.2d 184,
27 187(1979); *Ariz. Corp. Comm'n v. Woods*, 171 Ariz. 286, 296, 830 P.2d 807, 817 (1992) ("The
28 Commission was not designed to protect public service corporations and their management, but
rather, was established to protect our citizens from the results of speculation, mismanagement and
the abuse of power.").